THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION

DEPARTMENT OF TELECOMMUNICATIONS & ENERGY

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November 12, 1999

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie Roman Salas, Secretary
Federal Communications Commission
Portals II, 445 12th Street SW, Suite TW-A325
Washington, DC 20554

In the Matter of	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Low-Volume Long Distance Users	)	CC Docket No. 99-249
	)	
Federal-State Joint Board On Universal Service	)	CC Docket No. 96-45
	)	

Dear Ms. Salas:

Enclosed for filing in the above matter please find one original and five copies of the Massachusetts Department of Telecommunications and Energy's Comments in Support of the CALLS Plan. I have filed a copy of these comments electronically with the Commission's ECFS service in the proceedings listed above.

Sincerely,

Paul B. Vasington

Paul B. Vasington
Commissioner

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Before the
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MASSACHUSETTS DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY'S COMMENTS ON THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE PLAN

Commonwealth of Massachusetts
Department of Telecommunications and Energy

Janet Gail Besser, Chair
James Connelly, Commissioner
W. Robert Keating, Commissioner
Paul B. Vasington, Commissioner
Eugene J. Sullivan, Jr., Commissioner

One South Station
Boston, MA 02110
617-305-3500

Dated: November 12, 1999

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MASSACHUSETTS DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY'S COMMENTS IN SUPPORT OF THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE PLAN

The Commonwealth of Massachusetts Department of Telecommunications and Energy (MDTE) respectfully submits to the Federal Communications Commission (FCC or Commission) the following initial comments on the Coalition for Affordable Local and Long Distance Service (CALLS) Plan. These comments are in response to a Notice of Proposed Rulemaking issued by the FCC on September 15, 1999.

The MDTE is the Massachusetts administrative agency with general supervisory jurisdiction and control over telecommunications common carrier services offered within the Commonwealth of Massachusetts, pursuant to Massachusetts General Laws c. 159, § 12. The MDTE's address is One South Station, Boston, Massachusetts 02110.

I. INTRODUCTION

The CALLS Plan presents an historic opportunity for the FCC in one stroke to promote several of the still-elusive goals of the Telecommunications Act of 1996. The CALLS Plan would reform the pricing system for interstate access to bring it more in line with the underlying cost structure. The CALLS Plan would target subsidies for social policies in an explicit manner that is consistent with the Act and more conducive to competition and investment than the current implicit pricing subsidies. In doing so, the CALLS Plan advances the policy goals of competition, universal service, investment in advanced technology, and simplified customer bills. Moreover, the CALLS Plan advances these goals in a way that avoids the litigation that has plagued all concerned since passage of the Telecommunications Act of 1996 (Act).

Essentially, the CALLS Plan would accomplish the following:

- Interstate access rates over time would be more closely aligned with underlying costs by: 1) reducing the interstate, per-minute access charges; 2) increasing and consolidating the subscriber line charge (SLC) with other common-line charges; and 3) de-averaging and capping the subscriber line charge.

- Universal service support currently embedded in interstate access would become explicit and would thus better target low-income and high cost customers. This is accomplished by increasing the Lifeline discounts and by providing explicit funding to areas where the federal share of forward-looking loop and port costs exceed the capped SLC.

The Commission and many others have acknowledged that there are implicit subsidies in the interstate access rate structure. As the CALLS proponents note, in 1997 the Commission identified three forms of implicit universal service support in access charges: 1) geographic rate averaging between high and low cost areas; 2) support for residential service through higher charges on business lines; and 3) higher, above-cost usage charges to support costs of serving low usage subscribers (Memorandum in Support of the Coalition for Affordable Local and Long Distance Service Plan (CALLS Memo), pp. 4-5, citing Federal-State Joint Board on Universal Service, Report and Order, 12 FCC Rcd 8776, 8781 (1997) at ¶ 11). Over time, the Commission has endeavored to reduce the magnitude of these implicit subsidies via rate restructuring and the creation of the SLC. Subsidies remain, however, and Congress has indicated that "any support mechanisms continued or created under new section 254 [universal service] should be explicit, rather than implicit as many support mechanisms are today" (Telecommunications Act of 1996, Joint Explanatory Statement of the Committee of Conference).

II. DISCUSSION

A. The CALLS Plan Would Promote Efficient Competition For All Customers

Efficient competition benefits all customers. It leads to greater variety of better goods and services at lower prices. However, government-mandated pricing subsidies hamper—and may stifle—competition, and thereby deny its benefits to customers. Over the longer term, the perceived harm from the loss of subsidies for certain customers is likely to be outweighed by the benefits that these same customers will receive as a result of competition.

Where subsidies for achievement of social policies are deemed necessary, it is appropriate to make them explicit, because implicit rate subsidies are inconsistent with the development of efficient competition. Efficient competition occurs only when customers can make choices on the basis of competing firms' incremental costs and service quality. Pseudo-competition in the form of arbitrage will develop with the existence of implicit subsidies, but it will develop only (or predominately) for the customers, geographic areas, and services that are providing the implicit subsidies. With the existence of implicit subsidies, competitors are able to offer prices that are lower than the incumbent's regulated prices for customers whose rates are providing subsidies, but there is no way of knowing if these competitors' costs are lower than incumbents' costs. Thus, such pseudo-competition is not likely to result in the societal welfare gains that efficient competition would provide.

The CALLS Plan would promote the development of efficient competition for *all* customers by gradually replacing implicit subsidies with portable, explicit subsidies. It is crucial that the explicit subsidies be portable among competing carriers so that all carriers have an opportunity to offer services to subsidized customers. Otherwise, subsidized customers effectively will be locked into their incumbent carrier's service, even after implicit support is made explicit.

The economic reality is that competition will not develop for customers, geographic areas, and services that are subsidized, unless such subsidies are explicit and portable. However, competition in the form of arbitrage—coming in part from Internet-based services—will force the reform of pricing at some point with the necessity of raising prices for subsidized customers. The issue before us then is whether we as regulators reform pricing as a reaction to competitive pressure, or whether we instead deal with the problem up-front, on a more controlled and gradual basis, as the CALLS Plan does.[1]

B. The CALLS Plan Is Consistent With Universal Service

The CALLS Plan would not harm—and would in fact promote—the policy goal of universal service. The MDTE has engaged in rate restructuring for the incumbent local exchange carrier similar to that proposed by CALLS and has seen significant benefits from reducing implicit subsidies—all with no adverse effect on universal service. We are confident that adoption of the CALLS Plan would result in similar benefits at the national level without any negative effect on universal service. In fact, as the CALLS proponents noted (see CALLS Memo, pp. 16-17, n.36), a number of recent academic studies indicate that payments for usage may have a bigger effect on universal service than do fixed monthly payments. Seen in this light, adoption of the CALLS Plan would, in fact, promote universal service.

The Massachusetts experience with rate restructuring should be instructive for the FCC as it evaluates the CALLS Plan. In 1985, the MDTE recognized that implicit rate subsidies are inconsistent with the development of efficient competition. The MDTE stated that "properly

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[1] In a recent paper, Dr. Joseph Farrell, former Chief Economist of the FCC from January 1996 to June 1997, stated that making unbundled network elements (UNEs) available at cost-based regulated prices will help to reform retail price regulation, which, he says, "has proven extraordinarily difficult both administratively and politically." (See Dr. Joseph Farrell, Economic Concerns Regarding Unbundling Broadband Cable Internet Access, March 19, 1999, pp. 2-3) If the FCC hopes to use its pricing methodology for UNEs as a tool for promoting more efficient retail prices for local exchange service, which is largely under the control of state regulators, it should lead by example and reform inefficient pricing under its own jurisdiction, as it did after divestiture with the creation of the SLC.

defined incremental costs should be used as the primary basis for pricing all services, including local exchange service," and announced that "to the extent that current rates do not reflect an appropriate allocation of costs, the [MDTE] will, consistent with the need to avoid major discontinuities in rate levels, move toward that goal" (D.P.U. 1731 (1985), pp. 36-38).

The MDTE pursued this policy line from 1986 to 1994. After conducting a traditional rate case and developing an appropriate marginal cost study, the MDTE rebalanced rates significantly, and, in doing so, made the following changes:

- Rate groups and message units were eliminated, so that all customers in every exchange pay the same rate for basic network access and local usage.
- Local calling areas were increased to a minimum of a customer's home and contiguous exchanges.
- Business rates for basic network access were reduced.
- IntraLATA toll and local usage rates were reduced for residence and business customers. Mileage differentials for intraLATA toll rates were eliminated in the 413 LATA.
- Carrier switched access rates were reduced to an average of about 3¢ per minute.
- Residential rates increased for basic network access (dial-tone) from about $3 per line, per month to $9.91 per line, per month.

These changes were greater in magnitude than those contemplated in the CALLS Plan, but—contrary to dire predictions that were made at the beginning of the process—did not adversely affect universal service in Massachusetts.

There has been no statistically significant change in Massachusetts's overall household penetration rate for telephone service since the beginning of the rate rebalancing. It is fair then to say that the significant rate rebalancing that took place in Massachusetts, in concert with the Commission's own rebalancing of the interstate access rate structure, had no detrimental impact on universal service. Instead, customers have seen significant benefits in the form of a simplified, standardized rate structure, much lower toll and access rates, and indirect economic development benefits derived from having lower business rates. In addition, we believe that the resulting, more economically-efficient cost structure has promoted the entry of competitive carriers in Massachusetts.

C. The CALLS Plan Would Promote Investment in Advanced Technology

The CALLS Plan proponents note that removing fixed-cost recovery from per-minute usage charges would reduce the artificial arbitrage between Internet Protocol-based services and regulated telephony (see CALLS Memo, pp. 13-14). But the benefits extend further: dissociating fixed-cost recovery and usage charges would also promote investment by regulated telephone companies in advanced technologies, such as DSL and ATM and photonic switching. To the extent that regulated telephone companies are reliant on toll and access usage charges to meet their total revenue requirement, these companies are less likely to invest in and develop new, packet-based services, which generally are priced on a flat-rate basis. This adverse effect is particularly visited upon rural and high-cost regions where fixed charges currently pick up a proportionately lower level of fixed costs.

In addition, litigation has held up many policy initiatives since passage of the Act and has created a large degree of regulatory uncertainty. The CALLS proponents note that "[t]he regulatory uncertainty that has characterized telecommunications markets since the 1996 Act will continue to 'overhang' all investment decisions, chilling investment and delaying the expansion of competition into residential and rural markets." (CALLS Memo, p.5). Resolving so many contentious issues via a negotiated settlement, as the CALLS Plan does, reduces this uncertainty to the point that it should not be a significant factor in capital investment.

D. The CALLS Plan Would Simplify Customer Bills

The CALLS Plan would eliminate Primary Interexchange Carrier Charges (PICCs), which are billed to interexchange carriers and often passed on to customers, and would consolidate them with the SLC. The CALLS Plan would thereby simply customer bills and reduce customer confusion related to the increasing number of fees and charges on their bills. Moreover, a lot of customer time and effort is now spent using dial-around services and other bypass opportunities to avoid these charges. Consolidating these charges in a more understandable manner would free customers from the need and inconvenience of fee-avoidance practices. In addition, the CALLS Plan over time would eliminate the price difference in SLCs for primary and non-primary lines, which was put in place by the FCC several years ago. Charging a higher SLC on non-primary lines has created confusion about distinctions between primary and non-primary lines and has resulted in the derogatory label of a "modem tax" being tagged on the higher SLC for non-primary lines. Customers would no longer need to differentiate between primary and non-primary lines and the modem tax label would disappear if the CALLS Plan were adopted.

III. CONCLUSION

Because we price fixed network access prices below efficient levels and make up the difference by over-pricing usage charges, the existing telephone pricing system of implicit subsidies, in essence, works on the premise that we subsidize customers' access to the network by over-charging them for actually using it. This is not appropriate anymore (if it ever was) with the growing importance of communications technology in what is often referred to as the Information Age. And it is not appropriate to the shared state and federal policy goal of introducing competition and other market mechanisms. Customer benefits cannot be measured exclusively by the fixed, monthly charge that residential customers pay. Instead, benefits should be viewed more broadly in terms of promoting competition and investment, which is what the CALLS Plan does. Moreover, the intent of Congress is to promote competition and to provide for social policy goals via explicit funding. Quick approval of the CALLS Plan would be among the most significant actions taken by any regulatory body or court, since passage of the Act, toward finally achieving the goals of the Act.

Respectfully submitted,
Massachusetts Department of
Telecommunications and Energy

By:

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James Connelly, Commissioner

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